Sanitized Copy Approved for Release 2011/03/07: CIA-RDP97-00771R000707060001-2



Secret -	
	25 X 1

file copy de not renove

International Economic & Energy Weekly

25X1

29 June 1984

Secret-

DI IEEW 84-026 29 June 1984



	Secret
•	
,	International
	Economic & Energy
•	Weekly
	29 June 1984
iii	Synopsis
1	Perspective—South American Debt: After Cartagena
3	Briefs Energy
	International Finance
	Global and Regional Developments
	National Developments
19	South America: IMF Austerity Under Attack
19	Spatii America. Tivit Austerity Onder Attack
25	LDC Debtors: Incentives for Moratoriums
21	To the left of Division of Div
31	International Financial Situation: Political Update This article was prepared by analysts from OEA, ALA, and OGI.
	This direct was prepared by diffusios from OLM, ALM, and OGI.
33	International Financial Situation: Debt Arrearages
. \	
37	International Financial Situation: Comparison of Adjustment in Eastern Europe and Five Major Debt-Troubled LDCs
	Eustoni Burope and Tive Major Beet Housed EBes
41	The Soviet Grain Crop: Impact on Imports and Meat Supplies
· ·	
	Comments and queries regarding this publication are welcome. They may be
	directed to Directorate of Intelligence, telephone

•	Secret
•	
	International
	Economic & Energy
	Weekly
	~ .
	Synopsis
•	
1	Perspective—South American Debt: After Cartagena
•	
	The emphasis during the Cartagena conference on political solutions to
	alleviate debt burdens will put new strains on international rescue programs in
	the coming months.
19	South America: IMF Austerity Under Attack
	Severely strained economic conditions and sharply reduced living standards
	are prompting South American governments to question whether IMF-
	supported austerity programs are acceptable.
25	LDC Debtors: Incentives for Moratoriums
	The dropoff in new lending to debt-troubled LDCs over the past five years is
	reducing economic incentives to meet interest and principal payments.
31	International Financial Situation: Political Update
•	IMF austerity measures have led to heightened political tensions in a number
	of Latin American countries this past month.
33	International Financial Situation: Debt Arrearages
	At least 54 LDCs and East European nations currently are behind on their
	debt repayments, slightly more than the record total of 52 at yearend 1983.
•	Most of the arrearages are accounted for by a handful of major debtors.
27	The state of the s
37	International Financial Situation: Comparison of Adjustment in Eastern Europe and Five Major Debt-Troubled LDCs
	Eastern Europe and Five Major Debt-Troubled LDCs
	Eastern Europe appears to be adjusting to its debt crisis more rapidly than
	most of the LDCs. The quicker turnaround for Eastern Europe results from
	being forced into adjustment earlier and the region's comparatively smaller
	financial problems.
41	The Soviet Grain Crop: Impact on Imports and Meat Supplies
	The size of this year's grain crop is likely to lead to higher grain imports than in 1983 and could jeopardize the Soviet's effort to match last year's record
	IN LAKE AND COULD INCOMPTOIZE THE NOVINT'S RELOTE TO MATCH 19ST VEAT'S TROUT

iii ·

	Secret
	International
	Economic & Energy
	Weekly
	29 June 1984
	29 June 1904
erspective	South American Debt: After Cartagena
	The emphasis during the Cartagena conference on political solutions to
	alleviate debt burdens will put new strains on international financial rescue
	programs in the coming months. The final communique not only emphasizes
	the need for a political solution to the debt problem, but also criticizes rising
	interest rates and growing protectionism by industrial countries. The Latin
	America foreign and finance ministers also called for more flexible IMF
	conditions and measures to help ease the repayment burden. We believe
	Cartagena marks a key turning point. Even though a formal debtors' cartel did
	not materialize, we believe the Latin countries will be more inclined to use po-
	litical pressure to attempt to obtain repayment concessions, a development that
	poses dangers for the current approach to the debt problem.
	The Cartagena Consensus is the first concrete step in taking a unified stand on
	debt issues. The creation of a consultative system will enable the Latin debtors
	to coordinate their actions more effectively by sharing information on debt
	negotiations. Moreover, it indicates a heightened political willingness to press
	for financial reforms. Although Brazil and Mexico were eager to avoid any
	move that would appear confrontational, the selection of Argentina as first
	coordinating secretary indicates Latin debtors could yet resort to tougher
	actions. In our view, the Argentines, having received support at Cartagena,
	may adopt more hardline tactics with bankers.
	We believe debt management will increasingly become a political issue. Latin
	American leaders will press, as a group, the governments of the industrial
•	countries to take a more active role in easing the debt burden. They are likely
	to seek official intercession with the IMF for policies designed to revive growth
	in an attempt to ease social unrest and with private banks to extend repayment
	concessions. They will also seek greater access to import markets in the
	industrialized countries and larger credit lines from international lending
•	agencies.
	The major debtors are probably well aware that the gradual transformation of
. "	debt management into a political issue is a double-edged sword, and could
	undermine access to new money and hurt ongoing negotiations. If debt
	management becomes a highly politicized issue, debtor countries may suffer.
	Unwillingness to work with the IMF—best exemplified by Argentina's
	unilateral decision to present a program to the Executive Board—may reduce

the willingness of bankers to lend because their financial support is contingent on economic adjustments. At the same time, bankers' reluctance to reduce

> Secret DI IEEW 84-026 29 June 1984

interest rates to levels sought by some debtors is likely to cause Latin American governments to put increased pressure on the governments of	
creditor countries—particularly the United States—to intervene.	
It is increasingly likely that debtor countries will subordinate necessary economic adjustments to domestic political considerations. The smaller debtors in particular could opt for political expedients and, in the process, undermine creditors' continued cooperation in making new loans and rescheduling debts to all countries in the region. This judgment is based, in part, on reactions to Bolivia's unilateral suspension of payments in late May, a move aimed at placating labor restiveness. Although the actual repayment amounts were small, bankers fear that this could set a dangerous precedent. Unilateral action by one debtor could set in motion a chain reaction among other small debtors.	
We speculate that Colombia, Peru, and Ecuador are the most likely candidates to declare unilateral payments moratoriums in the coming months: • With Colombia's liquid foreign exchange reserves equal to about one month of imports, President Betancur—who is still resisting an IMF agreement—may be tempted to suspend payments abruptly. • Growing domestic political and labor pressures during the presidential election campaign may cause Peruvian President Belaunde to pursue hard-line tactics. • Ecuador's conservative President-elect Febres Cordero, who has publicly said he will pursue better debt renegotiation terms, could suspend debt servicing to improve his standing with labor and the left.	•
We believe the smaller debtors—acting individually but moving in the same direction—could adopt confrontational tactics to try to force major concessions from lenders. We believe these countries, spurred by Argentina's recent example, could present programs to the IMF on a "take it or leave it" basis. We also believe these debtors may demand new loans from bankers at fixed interest rates and with repayment periods of 15 years or more. The more rebellious debtors also could demand that lenders capitalize interest payments or place a cap on total interest payments to insulate them from interest-rate increases.	
Major Latin American countries have little leverage to head off unilateral payments suspensions by smaller debtor countries. Despite the risks, the major debtors may even tacitly support such moves in the hope of benefiting from any concessions granted by creditors. Any easing of commercial repayment terms, for example, would probably cause Brasilia and Buenos Aires to strengthen their determination to obtain a multiyear restructuring package on easier terms.	
	,

25X1

25X1

25X1

25X1

25X1

25X1

Briefs

Energy

Big[°] Seven Oil Consumption Increases Dramatically Oil consumption in the seven major developed countries rose nearly 6 percent in first quarter 1984 over year-earlier levels—the first quarterly increase since 1979. The increase in oil consumption reflects the economic expansion in the Big Seven countries. Consumption of most major products increased as gasoline, diesel fuel, and light fuel oil sales in the seven countries rose 10 percent, 11 percent, and 8 percent, respectively. Sales of heavy fuel oil increased in the United States and Japan but continued to decline in Canada and Western Europe.

Major Developed Countries Oil Consumption

Percent change a

25X1

25X1

25X1

25X1

25X1

	1980	1981	1982	1983	1984
Big Seven	-7.9	-7.5	-6.3	-5.7	5.8
France	-11.1	-10.0	-11.8	-3.2	3.2
Italy	-2.3	-11.0	-9.8	-3.3	1.5
United Kingdom	-14.5	-14.2	4.9	-9.4	2.6
West Germany	-7.2	-10.4	-5.5	-4.9	0.5
Canada	-0.2	-8.1	-6.0	-15.6	0.6
Japan	-4.0	-7.5	-5.3	-4.3	10.4
United States	-9.3	-7.9	-6.6	-5.5	6.7

a Percent change from corresponding period (first quarter) one year earlier.

West European Gas Vse Surges

Preliminary data indicate a sharp increase in West European gas demand during the first quarter of 1984. Gas use in West Germany—Europe's largest consumer—rose 15 percent, while the United Kingdom and France experienced increases of 8 and 11 percent, respectively. In Italy, industry officials expect a 15-percent increase in gas use this year and have indicated that first-quarter results exceeded their expectations. Increased West European gas use results principally from increased residential consumption caused by the cold winter and higher industrial use resulting from the economic recovery. Gas use also is up in electric utilities—particularly in Italy and France—as utilities attempt to reduce excess supplies resulting from take-or-pay contract provisions.

25X1 25X1

25X1

25X1

25**X**1 25**X**1

25X1

25X1

25X1

OPEC Concerns About Market Outlook	Attendees at the late May meeting of OPEC's Board of Governors expressed deep concern over the stability of the cartel unless there is an upturn in crude oil demand and prices in the page term	
	oil demand and prices in the near term,	•
	senior Nigerian oil official recently told the US Embassy that unusually high	
	consumer stockbuilding in the second quarter has made it unrealistic for Nigeria to request an increase in its quota. The official now puts demand for	
	OPEC oil at about 18 million b/d in the second half of this year, or nearly	
	1 million b/d below earlier expectations. We do not expect any adjustment in	
•	OPEC quotas at next month's meeting even though some members, including Nigeria and the UAE, may press for higher output. Given prospects for	
	continued weak demand, OPEC will face growing difficulties in preventing	
	downward price pressures unless events in the Persian Gulf cause a significant	
	disruption in oil supplies.	
	, 	25
Darhage to Khark	The Iraqi air attack on 24 June damaged a portion of Khark Island's four-	20
Isfand	berth Sea Island terminal the southernmost mooring dolphin—which is used to align loading tankers—sustained some	
	minor damage. The helipad serving it, however, is extensively burned and	
	probably unusable. Although loading capability of the terminal should be	
	unaffected, Iran has not loaded from this terminal since the attack. Inspection and repairs to the damaged facilities should not take more than a few weeks.	
	and repairs to the damaged resintes should not take more than a few weeks.	
٠. ا	Because the damaged dolphin was at the end of the Sea Island terminal, its loss is less critical than if it were closer to the load-	
	ing platform.	
		•

Secret

Japan To Take Equity in Australian LNG Project	Mitsui and Mitsubishi last week announced their intention to take a one-sixth equity interest in Australia's \$2.5 billion Northwest Shelf LNG project. Canberra still must approve the arrangement, which will reduce the Australian equity share to about 33 percent, well below the government's 50-percent guideline for resource projects. We believe, however, that the project's potential to generate \$1.5 billion a year in export earnings makes Canberra's approval almost certain. The Japanese investment should help secure LNG export contracts with Japanese utilities that could be signed by the end of the year.
	International Finance

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000707060001-2 $\bf Secret$

25X1

25X1

25X1

25X1

25X1

25X1

New Loan for Chile	Chile obtained a \$780 million bank loan in mid-June after the Finance
7	Minister agreed to comply with the existing IMF program and gave reassur-
/	
/	ances that Santiago would continue only cautious reflationary policies. The
<i>,</i>	nine-year loan includes a five-year grace period and carries an interest rate 1.5
	percentage points above US prime—a hefty reduction from the 2.25 percent-
·	age points over prime on last year's credit. According to Embassy reports,
	Chile was seeking disbursement of the first two tranches totaling \$390 million
	by the end of June. The delay in obtaining the loan—Santiago expected the
	first \$195 million tranche in April—has strained Chile's reserves. To prevent
	large drawdowns, the government used the remaining \$250 million of the \$550
•	million BIS credit for 1983-84, according to US Embassy reports.
	minor pie crear for 1905 of, according to 50 Emocassy reports.
·	C1 '1
	Chile continues to face severe financial difficulties. According to the US
· · · · · · · · · · · · · · · · · · ·	Embassy, Chile's trade surplus fell to \$372 million during January through
	April, down 12 percent compared with the same period a year earlier, mainly
• ,	because of depressed copper prices. We expect payments pressures will
	intensify in the second half of 1984.
	intensity in the second half of 1704.
	The Embassy reports that President Pinochet—
	angered by rising US interest rates and possible restrictions on copper
	imports—may be considering a more radial approach to dealing with Chile's
•	
	foreign debt.
•	
Jamajćan-IMF Update	Jamaica has met the last two preconditions necessary to qualify for \$144
	million in IMF loans. Last week Kingston reported the satisfactory renegotia-
	tion of debt owed to Trinidad and Tobago and announced 50- to 100-percent
•	· · · · · · · · · · · · · · · · · · ·
	price hikes for telephone service. According to the US Embassy, Kingston will
	use the first IMF disbursement to clear foreign payment arrears before
	approaching international bankers and official lenders to refinance at least
	\$300 million in debt.
	Labor's increasingly vocal demands for wage hikes to offset the inflationary
	effect of recent devaluations could quickly derail the new IMF program. The
	costly labor dispute that closed the Alpart alumina facility last month could
	spread to other bauxite companies that have not completed new contracts.
	Favorable settlements for the relatively well-paid bauxite workers could fuel
	demands of other unions, particularly public-sector workers. Tight government
	spending limits under the IMF program, however, will crimp Kingston's ability
	to fund civil service wage hikes. Public utility workers staged a two-day strike
	last week and have threatened to do so again unless the government concedes
	to wage demands. Opposition leader Michael Manley, president of a major
-	
* .*	labor union, is likely to push for further demonstrations against the govern-
~	ment's economic policy to keep pressure on the ruling party.

Cuban Debt Rescheduling Agreement Near	Cuba's creditor countries and commercial banks have agreed to reschedule Havana's \$365 million debt that falls due this year. Foreign payments and debt targets similar to those in last year's agreement were negotiated at a recent meeting with West European and Japanese Government creditors.	,
25X1		
	25X1	
Costa Rica Freezes Debt Payments	Delays in reaching agreement with the IMF for a \$52 million standby credit has prompted Costa Rica to secure a 90-day halt on principal payments to foreign commercial banks. A standstill agreement was reached with the banks on 15 June after it became clear that the IMF would not approve a standby by the 30 June deadline set by the banks. According to the US Embassy, the standstill agreement by itself is insufficient to stave off a foreign exchange crisis in July. Although USAID announced last week that it would disburse \$23 million, even the quick release of the remaining \$35 million in US aid scheduled for Costa Rica in 1984 would not cover the country's foreign exchange requirements through July. The banks now are requesting that Costa Rica raise domestic consumption taxes and clear arrears to the IMF to reach an agreement with the Fund by 31 August.	25X1
Hondurans Oppose IMF Preconditions	Growing labor opposition to austerity is making an IMF program for Honduras increasingly unlikely this year. To avert a strike last week by the country's largest union, President Suazo already has had to modify his recent economic stabilization package. Although the package still includes higher taxes and spending cuts, the IMF also is requiring devaluation or an expansion of the parallel foreign exchange market. Tegucigalpa strongly opposes a devaluation; the lempira's par value with the US dollar has not been changed for more than 50 years. With elections approaching in 1985, the Suazo government is reluctant to alter exchange rates because this would quickly boost inflation in this import-dependent economy.	25X
Suriname's Dim Aid Prospects	The US Embassy reports that Paramaribo may stall talks with the IMF and concentrate instead on restoring financial assistance from the Netherlands. A lack of preparedness by the Surinamese already has caused the talks with the Fund to proceed slowly. Moreover, policy measures proposed under an IMF agreement have received a cool reception. Business has rejected the Fund's call for devaluation, and labor has warned that strikes would follow any tax increases. The Dutch are the only other likely source for the level of funding needed by the cash-strapped economy. The Hague, however, continues to insist on an investigation into the murders of opposition leaders in December 1982—	25X
	•	

a condition for receiving aid that is strongly opposed by Army Commander Bouterse and others linked to the killings. Without significant aid inflows, pressure could quickly build on the government. Foreign exchange reserves have been nearly exhausted, and a virtual import ban has caused food shortages and cut deeply into living standards.

25X1

25X1

25X1

25X1

25X1

25X1

25X1

Moroccan-French Einancial Accord France's recent \$220 million loan and export credit package to Morocco provides badly needed support. This financing moves Paris ahead of Saudi Arabia as Morocco's foremost benefactor and reaffirms France's intent to remain Morocco's most important commercial partner. The US Embassy reports that the project aid is targeted at three priority development projects, and represents the Mitterrand Government's determination to support Morocco's economic stabilization program. The amount of assistance, however, is only a fraction of the \$2.5 billion in long-term support requested by the Moroccan Prime Minister during his mid-April visit to Paris.

Global and Regional Developments

EC Sammit Success

EC leaders have finally broken the budget deadlock that has paralyzed the Community for the past six months. British Prime Minister Thatcher agreed to a 1984 rebate of approximately \$800 million and to a formula for rebates in the following years of two-thirds of London's net tax contributions. With this agreement, Mrs. Thatcher will no longer block a nearly 20-percent Community revenue increase, which, because of the lengthy ratification process, probably will take effect in 1986. EC Finance Ministers will begin next month to consider interim financing measures. The Commission estimates that the Community faces at least a \$2 billion budget shortfall this year.

Although the rebate agreement takes the budget issue off the top of the EC's agenda, the EC still faces financial problems. The bulk of the new revenues will go to Spain and Portugal when they enter the Community, probably in 1986. Moreover, despite the much-touted dairy-sector reforms hammered out at the March EC summit, the Common Agricultural Policy remains a major financial drain.

Yugoslav-Westinghouse Countertrade Deal After lengthy negotiations, Yugoslavia and Westinghouse have agreed to a countertrade deal involving the financially troubled Krsko nuclear power plant built by Westinghouse. Yugoslavia will obtain spare parts, equipment, and services for the power plant. In return, Westinghouse will make a "best effort" to purchase up to \$15 million in Yugoslav goods and services in 1984-86. The Krsko management insisted on the deal because it lacks the funds needed to cover rising operating expenses and debt service, and Yugoslav authorities are pressing for countertrade arrangements to cover new hard currency outlays. Krsko does not earn hard currency from its domestic electricity sales and must depend on the Croatian and Slovenian republics to cover its foreign exchange

Secret

· · · · · · · · · · · · · · · · · · ·	for the project, and the Croatian and Slovenian governments will be hard pressed to meet the \$200 million in payments for Krsko this year. According to the US Consulate in Zagreb, Krsko officials also are under orders to press for countertrade commitments as a precondition for renegotiating the US-Yugoslav nuclear fuel enrichment agreement. The Yugoslavs reportedly have asked West European fuel processors for offers of fuel enrichment linked to countertrade.
Taiwan Planning Tariff Reductions	The Taiwan Government is studying large tariff reductions on more than 1,000 imported items. The plan is partly in response to US pressures on Taiwan to reduce its bilateral trade surplus, which reached \$6.7 billion last year. Past tariff cuts, however, have had little impact on US sales, and strong local opposition persists. Indeed, to protect local businesses and government revenues, Taiwan already has announced it will introduce any tariff reductions gradually and not start until 1985.
3%	
3% vd	

National Developments

Developed Countries

West German Economics Minister Resigns

Free Democrat Martin Bangemann will replace Count Otto Lambsdorff, who resigned as Economics Minister Tuesday. We do not expect major shifts in Bonn's economic policy, but Lambsdorff's absence may tone down West German criticism of US economic policies. Lambsdorff had long been expected to step down before coming to trial on charges of accepting bribes.

25X6

Compromise in West German Metalworkers' Strike

The chief arbitrator in the seven-week-old strike says that his compromise proposal for a 38.5-hour workweek probably will be acceptable to both sides, but management appears to be called on for greater concessions. The eightman arbitration panel must approve the proposal unanimously, and if it does, the union and the employers will have one week to accept or reject it. The proposal, to take effect next April and run for 18 months, entails a 1.5 hour cut in the average workweek, a 3.9-percent wage increase to preserve present pay levels, and an additional 2-percent raise. Workers also would receive a 3.3-percent pay increase starting next month and a \$90 lump-sum payment to cover the five-month period since the previous contract expired.

Union leaders probably will accept the compromise even though the goal of a 35-hour workweek would not be obtained. The agreement meets their demand for a shorter workweek with no cut in pay. Management, which has steadfastly resisted a retreat from the 40-hour week, probably will try to amend the proposal further as the talks continue. Employers also may want to stall until West Germany's supreme court rules on their appeal of a lower court ruling that nonstriking metalworkers idled by parts shortages are entitled to unemployment benefits. Unemployment pay for these workers would bolster union bargaining power considerably by stretching union strike funds.

The strike has idled 450,000 workers in West Germany and 25,000 in Belgium, the Netherlands, Italy, and Austria because of a lack of parts from the shutdown West German auto industry. Ford, GM, and Volkswagen have halted production in Belgium, and the BMW plant in Austria is closed. Should the strike continue, many more West European factories and auto dealers will be affected, especially in France, Spain, and Italy.

25X1

25X1

25X1

25X1

No End in Sight for	The coal miners' strike is nearly four months old, and no end is in sight.	
British Miners' Strike	Although becoming concerned over the economic impact of the dispute,	
	London has stated that it is prepared to see the strike through into next year.	
	The strike so far has shut down close to 80 percent of the country's mines,	٥٢١
**	caused London to trim its 3-percent expected growth rate for 1984 by 0.5	25)
	percentage points, and, according to some financial experts, has cost the	
· ·	government approximately \$1.4 billion. The Central Electricity Generating	
	Board has accelerated its coal, oil, and gas imports—contributing to a record	
	trade deficit for April and adding to pressure on the pound—to ensure against	
	major disruptions to the economy. Stocks of coal, excluding those held by the	
	industrial sector, fell by 7.2 million metric tons—or 13.5 percent—in the year	
	ending in March; 74 percent of this drop occurred from February to March,	
	when the strike began. Nevertheless, the National Coal Board—which makes	
	and implements coal policy in the United Kingdom—seems confident that	
<u> </u>	stockpiles can be stretched into fall.	25)
		20,
34 - 4 ⁷	The Railwaymen's Union has threatened to join the strike and stop all	
	shipments of coal and iron ore. If the transport unions support the miners,	
	efforts to distribute reserves to steel mills and power plants would be	
	hampered. London hopes that these recent statements of labor solidarity have	
	no more substance than those issued a few months ago when transport unions	
	pledged their support but most truckers and railwaymen continued hauling	
4	coal. There has been increased violence on the picket lines, and the government	
	is providing police protection for truckers carrying coal. The press is calling	
•	this the most violent labor dispute ever in Britain. It has thus far resulted in	
in the second second	two deaths, many injuries, and over 3,400 arrests. Public pressure is mounting	
	on both parties to resume talks—which have broken down twice—and resolve	
તું છ	the protracted dispute. Even though the strike puts a snag in Prime Minister	
	Thatcher's drive to reduce the budget deficit, she probably will oppose any	
•	accommodation with miners' chief Arthur Scargill, whom she sees as more	
	interested in damaging her government than in representing the interests of	
	the miners. Coal Board Chairman Ian MacGregor recently sent all members	
	of the miners' union a letter that questioned Scargill's motives and warned	
	them of the potential adverse impact of a protracted strike.	25)
		201
* * *		
Italian Góvernment	Italy's state-run air, rail, and maritime transport services have been hit by a	
Response to	series of short strikes, many in protest against Rome's inability to provide	
Transportation Strikes	promised economic benefits. Although the net economic loss thus far is small,	
	Rome nevertheless is concerned that the strikes could cut into the expected	
•	record tourism earnings needed to avoid a current account deficit this year.	25)
	Parliament, which in the past often has intervened to resolve labor disputes in	20/
	the transport sector, last week approved a new railworkers' contract and	
	appropriated extra funds for port workers. Public irritation over the strikes,	
:	however, may prompt Rome to seek greater control over the transport unions.	
	Some coalition members already have called for new labor regulations in	
	essential public services, and Christian Democratic Party leader De Mita	
	recently announced that his party soon will introduce such legislation.	25)

11

25X1

25X1

25X1

25X1

~ 25X1

25X1

25X1

25X1

French Austerity	After a first-quarter pause, inflation and trade seem to be responding to the Mitterrand government's austerity policies. The rate of inflation has fallen during the last two months, bringing the annual rate since the start of the year
∕ ∙	to 7.5 percent, well below the 11-percent rate for the same period in 1983. The
	trade balance recorded a small surplus in May, after larger-than-expected
	deficits in the first quarter. For the year, the trade deficit is running at an an-
	nual rate of about \$5 billion, half the rate for the same period in 1983. Progress on the inflation and trade fronts has been slower than the govern-
	ment's timetable
	Austerity
	continues to take its toll in jobs; unemployment is nearing 10 percent. In
	addition, household consumption and industrial production for the last three
	months are below the levels of the previous three months.
srgeli Wage Accord	The Histadrut, Israel's large organization of trade unions, reached agreement
	with the government last Sunday on a generous two-year wage pact for most
	government workers. The government caved in to most of labor's demands to
	avoid widespread strikes just before the elections on 23 July. Under the accord,
	wages will be increased 15 percent during the next few months on top of regular cost-of-living adjustments. The Israeli press reports, however, that a
	few public-sector unions, including the engineers and teachers, have rejected
	the agreement because it favors lower income workers. This pact will increase
	pressure on the Manufacturers' Association to reach a similar agreement for
	private-sector workers. The new accord also will increase real wages and add
	to inflation, now running at an annual rate of 400 percent. Any postelection
	government now will have greater difficulty in getting Histadrut to agree to
	wage limits as part of an austerity program.
	wage mints as part of an austerity program.
	wage minus as part of an austerity program.
Inkara Announces	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and
Iajor Public-Sector	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase
lajor Public-Sector	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase efficiency and strengthen his control over the public sector. Ozal says he has
lajor Public-Sector	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase efficiency and strengthen his control over the public sector. Ozal says he has abolished more than half of the committees, boards, and commissions within
lajor Public-Sector	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase efficiency and strengthen his control over the public sector. Ozal says he has abolished more than half of the committees, boards, and commissions within the various ministries. The new framework law for the SEEs—which replaces
lajor Public-Sector	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase efficiency and strengthen his control over the public sector. Ozal says he has abolished more than half of the committees, boards, and commissions within the various ministries. The new framework law for the SEEs—which replaces 32 separate laws—is intended to make the state enterprises operate more
lajor Public-Sector	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase efficiency and strengthen his control over the public sector. Ozal says he has abolished more than half of the committees, boards, and commissions within the various ministries. The new framework law for the SEEs—which replaces 32 separate laws—is intended to make the state enterprises operate more efficiently by eliminating several umbrella organizations and imposing mana-
lajor Public-Sector	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase efficiency and strengthen his control over the public sector. Ozal says he has abolished more than half of the committees, boards, and commissions within the various ministries. The new framework law for the SEEs—which replaces 32 separate laws—is intended to make the state enterprises operate more efficiently by eliminating several umbrella organizations and imposing managerial experience requirements for management positions. In addition, Ozal
lajor Public-Sector	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase efficiency and strengthen his control over the public sector. Ozal says he has abolished more than half of the committees, boards, and commissions within the various ministries. The new framework law for the SEEs—which replaces 32 separate laws—is intended to make the state enterprises operate more efficiently by eliminating several umbrella organizations and imposing managerial experience requirements for management positions. In addition, Ozal promised to submit to parliament legislation to abolish state monopolies in
Iajor Public-Sector	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase efficiency and strengthen his control over the public sector. Ozal says he has abolished more than half of the committees, boards, and commissions within the various ministries. The new framework law for the SEEs—which replaces 32 separate laws—is intended to make the state enterprises operate more efficiently by eliminating several umbrella organizations and imposing managerial experience requirements for management positions. In addition, Ozal
Iajor Public-Sector	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase efficiency and strengthen his control over the public sector. Ozal says he has abolished more than half of the committees, boards, and commissions within the various ministries. The new framework law for the SEEs—which replaces 32 separate laws—is intended to make the state enterprises operate more efficiently by eliminating several umbrella organizations and imposing managerial experience requirements for management positions. In addition, Ozal promised to submit to parliament legislation to abolish state monopolies in tobacco, tea, and alcoholic beverages. Ozal's reorganization follows through on campaign promises. The restructur-
Iajor Public-Sector	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase efficiency and strengthen his control over the public sector. Ozal says he has abolished more than half of the committees, boards, and commissions within the various ministries. The new framework law for the SEEs—which replaces 32 separate laws—is intended to make the state enterprises operate more efficiently by eliminating several umbrella organizations and imposing managerial experience requirements for management positions. In addition, Ozal promised to submit to parliament legislation to abolish state monopolies in tobacco, tea, and alcoholic beverages. Ozal's reorganization follows through on campaign promises. The restructuring of the SEEs is intended to make them more attractive to private investors;
Tajor Public-Sector Pebrganization	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase efficiency and strengthen his control over the public sector. Ozal says he has abolished more than half of the committees, boards, and commissions within the various ministries. The new framework law for the SEEs—which replaces 32 separate laws—is intended to make the state enterprises operate more efficiently by eliminating several umbrella organizations and imposing managerial experience requirements for management positions. In addition, Ozal promised to submit to parliament legislation to abolish state monopolies in tobacco, tea, and alcoholic beverages. Ozal's reorganization follows through on campaign promises. The restructuring of the SEEs is intended to make them more attractive to private investors; Ozal has pledged to sell several of them. The restructuring also provides Ozal
Inkara Announces Iajor Public-Sector Rebrganization	Prime Minister Turgut Ozal's major reorganization of the bureaucracy and the State Economic Enterprises (SEEs) last week is intended to increase efficiency and strengthen his control over the public sector. Ozal says he has abolished more than half of the committees, boards, and commissions within the various ministries. The new framework law for the SEEs—which replaces 32 separate laws—is intended to make the state enterprises operate more efficiently by eliminating several umbrella organizations and imposing managerial experience requirements for management positions. In addition, Ozal promised to submit to parliament legislation to abolish state monopolies in tobacco, tea, and alcoholic beverages. Ozal's reorganization follows through on campaign promises. The restructuring of the SEEs is intended to make them more attractive to private investors;

	Less Developed Countries	
Kuwait Restricts Currency Flight	Kuwait's Central Bank soon will require that all overseas transfers of \$850,000 or more be reported and is considering restrictions on the flow of cash abroad. The Central Bank already has implemented a two-tier exchange rate for dollars to make the transfer of dollars abroad more difficult. Kuwaitis, who traditionally have held large balances of Kuwaiti dinars at local banks, are converting dinars to dollars and moving the money overseas because of uncertainty about the course of the Iran-Iraq war and lack of suitable local investments. US Embassy sources estimate that currently as much as \$1.4 billion is leaving Kuwait monthly, compared with \$600-680 million a month in 1983. We doubt the Central Bank's new policies will substantially reduce the	25)
	outflow of money.	25)
UAE Budget Logjam Nears Resolution	After heated debates among the United Arab Emirates on funding the 1984 budget, Abu Dhabi appears to have given in and will bear most of the costs. The prolonged budget maneuvering, particularly between the richer emirates of Abu Dhabi and Dubayy, had threatened to push the loosely unified federation further apart. Although Dubayy originally agreed in principle to spend 50 percent of its estimated \$3 billion or more of oil income on the federal budget, it later temporized. To resolve the deadlock, the UAE's President, Shaykh Zayid from Abu Dhabi, accepted a Dubayy contribution of only \$545 million, and Abu Dhabi pledged \$3.5 billion to fund the budget, according to the US Embassy in Abu Dhabi. In addition, Abu Dhabi will pay about \$550 million to cover overdue bills to contractors and government employees.	25) 25) 25)
		25X1
	Abu Dhabi's funding probably was meant to shame Dubayy into providing more money, although we doubt Dubayy will do so. In any event, the move buys support for Abu Dhabi from other poorer emirates in the north. Moreover, UAE merchants will welcome Abu Dhabi's decision to relieve the liquidity squeeze and instill confidence in a local economy that is heavily dependent upon government expenditures.	25X
Record Saudi Wheat Crop	This year's Saudi wheat crop is expected to reach a record 1.3 million metric tons, according to recent US Embassy reporting. Moreover, the Embassy projects the 1985 crop could hit 2 million tons, and as much as a million tons may be available for export next year. Riyadh has achieved self-sufficiency in wheat—as recently as 1980 it imported over 1.3 million tons—by guaranteeing farm support prices at four times world market levels, but the program has caused problems: • Despite a 12-percent increase in this year's subsidy budget, there may not be sufficient funds to pay farmers for the entire crop. Payments for part of the 1983 crop were delayed until March 1984, and similar delays are expected this year.	25)

13

• Although the Saudis have doubled wheat storage capacity in the past two years, up to 400,000 tons will have to be stored in temporary bins and trucks this season

25X1

25X1

25X1

25X1

25X1

25X1

- The government lacks transport facilities to export large volumes.
- The increase in farm acreage is rapidly depleting nonrenewable water resources.

Saudi Arabia's wheat surplus is a symptom of the growing difficulty for commodity markets caused by subsidies and technology. By using the latest seeds, fertilizer, irrigation, and foreign know-how, Saudi Arabia has achieved wheat yields on a par with those in the United States and the European Community. The Saudis now will have to dispose of their excess wheat in an already glutted market. Although Saudi officials are reducing wheat subsidies and considering diversification into other crops, we believe subsidies will remain at levels that encourage overproduction.

Pakistan Mandates Islamic Banking Finance Minister Ghulam Isahq has announced that Pakistan will eliminate the use of interest in its financial system by 1 July 1985. Although the precise mechanics of the conversion have not been announced, Isahq said that all deposits will be on a profit and loss sharing basis and that the new system will apply to all financial institutions operating in Pakistan, including foreign banks. State-owned banks and one foreign bank have offered an optional form of an interest-free account since January 1981 that has depositors share in the profit/loss of investments financed by these deposits. The US Embassy reported earlier this year that these deposits account for about 13 percent of total deposits. The government has established minimum rates of return for profit-sharing accounts in nationalized banks equal to or higher than the minimum rates prescribed by the State Bank for regular interest-paying deposits.

The setting of a specific date for an end to interest is a direct bid by the government for the support of religious fundamentalists in elections anticipated later this year. The fundamentalists have criticized President Zia for moving too slowly on Islamic measures. The government runs the risk, however, of committing itself to a system before it has figured out how the new system will handle many financial transactions, both foreign and domestic.

Economy Returning to Normal in India's Punjab The Indian Army attack on the Sikh's Golden Temple and subsequent occupation of the Punjab preempted a farmers' strike, which threatened to halt grain shipments following a record harvest. According to press reports, rail and road traffic has resumed, most curfews have been lifted, and crucial grain shipments have begun from India's leading foodgrain-producing state. The enforced peace has also allowed farmers and migrant laborers—primarily Hindus—to return to the fields to begin transplanting the winter rice crop. With key Sikh political leaders and many militants killed or jailed, a sense of stability reportedly has returned to the state. Nonetheless, the economic issues

Secret

that helped propel the Sikh protest movement—requests for higher food-grain procurement prices, increased water availability, and lower power rates—are yet to be resolved and agitations are likely to erupt again. We believe New Delhi will probably maintain a military presence in the Punjab for the remainder of the year, in part, to secure communications, protect Hindus, and restore local administration that was disrupted by the prolonged disturbances.

25X1

Communist

China's Winter Wheat Outlook Improves

Weather data show that increased rainfall in the winter wheat growing region has alleviated drought, prompting Chinese officials to predict another good wheat harvest. We believe that increased acreage and the improved weather could produce a crop this year comparable to the record 81 million metric tons harvested last year. The area sown to winter wheat, which accounts for 85 percent of the wheat crop, was expanded by 3 percent this year, according to Chinese press reports. Prospects of a bumper crop make it unlikely that China will take delivery this year of the 14 million tons of grain it has agreed to import from various sources, including 8 million tons from the United States.

25X1

25X1

Castro Shuns CEMA Summit

25X1

only party leader absent, a slight that apparently offended the Soviets. The Cuban delegation was headed instead by Castro's chief foreign and economic policy adviser, Vice President Rodriguez. An East European diplomat told the US Interests Section that, during planning for the summit, Cuba had expressed the hope of adjusting its economic development policy to emphasize industrialization. These plans apparently were rejected, because in his remarks

Castro's assessment that Cuba would not obtain economic concessions from

CEMA prompted him to skip the CEMA summit in Moscow. Castro was the

to the Cuban press after the summit, Rodriguez said Cuba will continue to fo-

cus its development on agriculture and mining.

25X1

Castro probably judged that the summit would produce no benefits and little hope for the Cuban consumer and did not want to associate himself directly with this outcome. He may hope to negotiate later with Moscow directly to obtain a better deal for Cuba. Continued emphasis on traditional commodity exports—such as sugar, nickel, and citrus fruits—will force Cuba into even greater dependence on the USSR and Eastern Europe for economic assistance because prospects for earning hard currency from these products are bleak. At the same time, Moscow has

become increasingly irritated over Havana's inefficient use of resources and is looking for ways to cut its assistance to its most expensive client. Negotiations for the level of Soviet and East European aid to Cuba during Havana's next five-year plan (1986-90) may result in less economic aid and more Soviet advisers to control its use. With Cuba facing the prospect of continued austerity for the remainder of the decade, economic relations with the USSR are likely to become more contentious as Havana looks for special treatment.

25X1



Sanitized Copy Approve	d for Release	2011/03/07:	CIA-RDP97	-00771R00070	07060001-2
------------------------	---------------	-------------	-----------	--------------	------------

Secret

Soviets Limit Fertilizer Exports		25X
		25X
	The emphasis on the Food Program apparently has shifted priorities in allocating fertilizer to agriculture rather than to exports. In 1983 agriculture received nearly 23 million tons of fertilizer nutrients, 14 percent more than in 1982; supplies of fertilizer to agriculture during 1976-82 grew at an average annual rate of only 2.2 percent.	25)

South America:	
IMF Austerity Under Attack	

Severely strained economic conditions and sharply reduced living standards are prompting South American governments to question whether IMFsupported austerity programs are acceptable. With all seven major South American debtor countries presently under or preparing for democratic civilian governments, economic austerity has become more difficult to sustain in the face of growing domestic discontent. To varying degrees, the governments of those countries that have undertaken austerity measures to gain IMF loans—Argentina, Brazil, Chile, Ecuador, and Peru—have begun to consider shifts to growth-oriented policies and a more radical approach to restructuring foreign debt payments. These countries at various times have fallen out of compliance with their IMF programs, but none have yet abandoned efforts to solve their problems under an IMF framework.

We believe, however, that debtors will demand increased flexibility on the part of the Fund and bank creditors to support domestic recovery. If such flexibility is not provided, some of these countries may confront the IMF with a "take it or leave it" demand for easier terms. Should cooperation between a debtor and creditors break down, then the chances are good that such a government would suspend its debt payments.

IMF-Supported Programs and Their Achievements

The current strategies coordinated under the IMF for correcting foreign payments imbalances and strengthening economic growth prospects in South American countries have rested on three pillars:

 The Fund has required that fiscal, monetary, foreign exchange, and pricing adjustments bring domestic demand in line with supply and that resources be shifted into exports.

- The Fund has counted on strong industrialized country recoveries, a rebound in commodity prices, and continued declines in global interest rates to facilitate improvements in current account balances.
- The IMF has been instrumental in securing the cooperation of foreign banks to provide new medium-term loans and the rescheduling of maturing debt.

According to US Embassy reporting, the seven major South American debtors—Argentina, Brazil, Chile, Colombia, Ecuador, Peru, and Venezuela—dramatically strengthened their foreign trade accounts in 1983. Collectively, their trade surpluses rose fourfold from \$3.6 billion in 1982 to \$18 billion. Nearly the entire adjustment burden fell to imports, which fell by more than one-fourth. Export earnings increased only negligibly because of depressed foreign demand and declining commodity prices. The impressive trade performances coupled with declining interest rates trimmed their combined current account deficit 60 percent to about \$12 billion in 1983.

Disappointment in 1983

The seven major South American debtor countries experienced a sharp fall in foreign capital inflows last year. Until the early 1980s, inflows of foreign loans greatly exceeded debt servicing and permitted South American governments to expand their investments and imports substantially. By 1983, outflows of principal and interest payments had begun to exceed the volume of new loans, compounding the severity of economic adjustment.

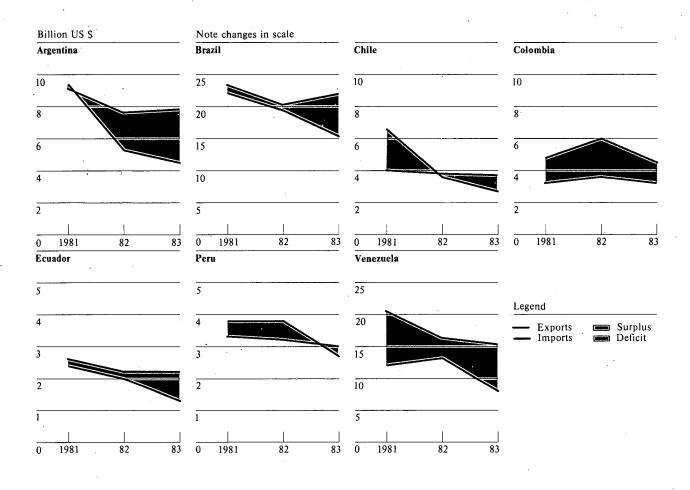
25X1

25X1

25X1

25X1

South American Trade Adjustments



303088 (A04832) 6-84

Contrary to South American government hopes, inflation accelerated in their countries in 1983. US Embassy reports indicate soaring prices became a particular concern in Argentina, Brazil, and Peru; all experienced triple-digit inflation. Currency devaluations and cuts in price subsidies under IMFsupported programs, poor weather, budget deficits, and plummeting popular confidence were the major causes of rising prices.

The South American recessions, moreover, deepened in 1983 because of increasingly restrictive

government policies to cope with rising inflation, continued sluggish foreign demand for South American exports, and the shrinkage in new foreign loans. Economic activity fell more than 3 percent in Brazil, Ecuador, and Venezuela, and plunged 11 percent in Peru—the largest declines experienced by these countries since the 1930s. In all major debtor countries, gross domestic investment stagnated.

25X1

25X1

Secret 29 June 1984 20

Major South American Debtors: Net Bank Loan Receipts

Billion US \$

•	1978			1981			1983		
	New Loans	Debt Service	Net Receipts	New Loans	Debt Service	Net Receipts	New Loans	Debt Service	Net Receipts
Argentina	3.8	2.6	1.2	10.3	4.4	5.9	6.3	7.0	-0.7
Brazil	17.0 -	8.4	8.6	15.3	15.3	0	12.4	13.1	-0.7
Chile	2.4 .	1.5	0.9	4.9	3.0	1.9	2.3	2.4	-0.1
Colombia	0.6	0.6	0	1.7	0.9	0.8	1.8	1.3	0.5
Ecuador	1.1	0.3	0.8	1.3	1.0	0.3	0.6	0.8	-0.2
Peru	1.3	0.8	0.5	1.6	2.0	-0.4	1.8	2.0	-0.2
Venezuela	4.0	1.6	2.4	4.1	5.0	-0.9	3.5 ·	4.0	-0.5

Major South American Debtors: Recent Economic Performance

Percent

	1980		1981	981 1982					1983			
	Inflation	Real GNP Growth	Invest- ment (as a Share of GDP)	Inflation	Real GNP Growth	Invest- ment (as a Share of GDP)	Inflation	Real GNP Growth	Invest ment (as a Share of GDP)	Inflation	Real GNP Growth	Invest ment (as a Share of GDP)
Argentina	88	0.7	24	131	-6.0	20	210	-5.7	17	345	2.8	17
Brazil	110	7.9	21 .	95	-3.5	20	99	1.0	19	211	-4.0	17
Chile	35	7.8	24	20	5.7	24	10	-14.1	14	28	-0.8	14
Colombia	27	1.9	NA	28	-0.1	NA	24	-1.0	NA	17	1.2	NA
Ecuador	13	4.9	. 24	16	4.5	·23	24	1.4	22	52	-3.4	18
Peru	59	3.0	18	75	3.9	22	64	0.2	20	111	-11.0	16
Venezuela	22	-1.7	29	16	0.4	30	10	0.6	30	6	-3.1	28

Living standards fell throughout the region last year, stirring increased popular discontent with prevailing economic policies. Real wage declines and high unemployment have hit the lower and middle classes especially hard. US Embassy reporting indicates large portions of the South American populations began having trouble meeting basic subsistence needs last year. Social frustration was

evident in the food riots and looting of supermarkets in Brazil and in the major strikes or demonstrations in Argentina, Chile, and Peru.

Financial adjustments have occurred while fledgling democratic governments and political movements have been trying to establish a firmer

25X1

25X1

footing. Democracy returned to Argentina in 1983 with the election of President Alfonsin. Brazil's military was preparing for presidential elections in early 1985 that will transfer control to civilians, and popular pressures for democracy have been mounting in Chile. Accordingly, the governments of major debtor countries have been increasingly obliged to heed public opinion in formulating economic policy.

Opposition to Austerity Reinforced in 1984

South American debtors, discouraged by economic deterioration and prospects of more of the same, became increasingly concerned in early 1984 that existing policy courses were ill advised. According to various sources, South American governments feared that weak commodity prices and import restraints in the industrialized countries will limit export growth and fuel domestic discontent.

Debtor disenchantment has become more pronounced since March, when the US prime rate and LIBOR—to which most South American interest payments are tied—began rising. Both interest rates have climbed 2 percentage points, increasing the foreign exchange cost of servicing debt. We estimate each percentage-point rise in interest rates adds roughly \$2 billion to the annual interest payments of the seven major South American debtors.

Rethinking Policy Strategies

According to a variety of sources, the experience of the past year is causing major debtor governments to reassess the IMF strategy and to consider alternative domestic-led growth plans. Nearly all South American leaders have underscored the importance of getting their economies growing again soon to prevent destabilizing political repercussions. Also, the major debtors are becoming worried that they will be unable to honor both their current debt payment schedules and sustain economic recoveries.

Argentina's newly elected President Alfonsin insisted early this year that foreign banks must offer more generous loan terms and that the IMF must allow greater latitude for growth. Although Alfonsin has pledged to seek an IMF agreement, he has criticized orthodox austerity remedies. Though acknowledging that domestic economic and foreign payments adjustments need to be made, he has stressed the importance of achieving 5-percent economic growth this year to preserve social and political stability. Time is running short, however, and the Alfonsin administration must reach an accommodation with the IMF before bankers will conclude an accord for new financing.

Political pressures have led Chile and Peru to sack key economic policy makers who had been staunch defenders of tough austerity policies. They have been replaced with advocates of more expansionary policies. The two governments are searching for policies that can restore growth and reduce unemployment but without sacrificing creditor support:

- Chile's new team under Economic Minister
 Collados has announced plans to speed recovery
 by increasing government public works spending.
- Peru's new Prime Minister Mariategui and Finance Minister Benavides have developed plans for a modest expansion of public spending. The IMF eventually accepted slightly easier terms, such as an increase in the public-sector deficit target for 1984 from 3.8 percent to 4.1 percent of GDP, and signed a new agreement in late April.

Despite IMF concessions, influential government officials in both countries continue to oppose the revised programs because they do not adequately stimulate growth. We believe both Santiago and Lima will come under political pressure and that difficulties lie ahead in their efforts to adhere to IMF guidelines.

25**X**1

25X1

25X1

25**X**1

25X1

25X1 25X1

Secret

In Brazil, domestic opposition to IMF-supported policies and growing debt service payments has continued to build. Brazil's most influential economists concluded recently that the combined effects of the growing debt payment burden and the IMF adjustment program will prevent economic recovery in the near term. Accordingly, the economists believe that major changes in government policies are essential. Moreover, all major candidates for the coming Brazilian presidential election advocate more stimulative domestic policies, revised IMF conditions, and a major restructuring of the debt.

Venezuela continues to resist recourse to an IMF loan program. Since taking office in February, the Lusinchi administration, flush with some \$11 billion in foreign exchange reserves, has effectively made the case that it wants no new financing from either the banks or the IMF but that it must secure refinancing for its 1983-85 debt payments. Caracas has designed an economic program to reduce foreign borrowing and set the economy back on a growth path.

Prospects

We believe most major South American debtor governments will soon find it necessary to ensure renewed economic growth and improved living standards in order to maintain political stability. If economic stagnation persists much longer under current policies, South America's budding democracies will be hard pressed to withstand social and political pressures for more expansionary policies.

Nonetheless, we believe that chances are good that the major debtors will maintain their IMF adjustment efforts and their debt servicing. This judgment is based on our expectation of substantial export growth over the second half of 1984 and into 1985. Moreover, we believe most South American governments recognize that continued commitment

to IMF or IMF-type policy strategies offers the least painful way to cope with large debts and sustain economic growth.

A major threat in the months ahead is posed by potentially higher interest rates. If the prime rate rises several more percentage points this year, as many bank economists are predicting, we believe the rise in interest payments will undermine South American debtor incentives to sustain domestic adjustments. Equally important, a surge in interest rates might limit the economic expansion in the industrialized world and sharply limit South American debtor hopes of generating additional export revenues.

If the South American political leaders come to believe the IMF strategy cannot meet debt and economic growth needs, they will shift, in our judgment, to expansionary policies and more domestically driven growth strategies. Some of the major debtors probably would be willing to proceed without Fund backing. The first major test is taking place in Argentina in the wake of President Alfonsin's direct program submission to the Fund's Managing Director of a counterproposal that emphasizes restoring growth. The temptation also will be strong for Brazil during its coming presidential succession to ease restrictive policies.

Implications

The abilities of the major South American debtors to gain better control over debt and economic recession will be critical to political stability in the region and continued strong intrahemispheric economic relations. Should some South American debtors choose domestically led growth policies over IMF stabilization programs, we believe this would portend more aggressive stands toward bank creditors. To sustain recovery, these countries are likely to insist on new debt payment formulas that would be explicitly linked to their ability to pay, regardless of the effects on bank profits. They probably would press creditors to stretch loan maturities to more than 15 years, establish grace

25X1 25X1

> 25X1 25X1

25X1

25X1

	Sanitized Copy Approved for Re	elease 201	1/03/07 : CIA	-RDP97-0077	1R0007070600	01-2
Secret	• • • . •					

periods for both principal and interest, and slash interest rates. We believe, in these instances, debtor governments would be willing to resort to temporary debt payment moratoriums to persuade creditors to be more responsive.

25X1

LD	C Debtors:	Incentives
for	Moratoriu	ms

25X1

The dropoff in new lending to debt-troubled LDCs over the past few years is reducing economic incentives to meet interest and principal payments and probably is increasing consideration of payments moratoriums. Last year, for example, several LDC debtors, including Mexico, Brazil, Argentina, Chile, and Venezuela, paid more interest on their foreign debts than they received in net new foreign loans, a dramatic reversal from the 1970s. For these countries, the foreign exchange cost of debt service now exceeds the foreign exchange benefits from new lending.

The Economic Incentive To Service Foreign Debt

It is hard to generalize about the causes of moratoriums because of the many economic and political factors that come into play, as well as the diverse nature of moratoriums themselves. Nevertheless, one key factor likely to figure into a debtor country's consideration of a debt moratorium is the level of interest payments on foreign debt compared with current and expected new lending. Interest payments are normally considered the price a borrower pays in order to have use of the lender's principal. Officials in a debt-troubled country, however, could take another view, if they assume that they cannot be forced to repay the principal already borrowed. From this viewpoint, payment of interest becomes the cost of maintaining an acceptable credit rating to secure new loans, rather than the cost of using borrowed funds.

Under this view, one indicator of a country's incentive to service foreign debt is the difference between new lending and interest payments over a

¹ In this article the term *net new lending*—or *new lending*—refers to loans made over and above the rollover of existing ones through rescheduling or other means. In addition, we have used just medium- and long-term debt figures because of the greater availability of historical data.

period of several years. This measure would suggest a weaker incentive for timely servicing of foreign debt if interest costs were higher and/or the volume of new loans were lower.

The step of declaring a complete moratorium on payments, however, is likely to be taken only as a last resort. The existence of formidable penalties—suspension of trade credits, trade disruption, seizure of assets, and loss of official funding—instead encourages countries to opt for milder actions midway between timely servicing and a total moratorium. These measures include:

- Moratoriums on principal payments that are made with the agreement of creditors.
- Running arrearages.
- Negotiations to obtain more official aid.
- Negotiations with creditors aimed at securing easier terms on outstanding debt and more borrowing.

Convergence of Interest Costs and New Borrowing

Using as an indicator the difference between new lending and interest payments, the economic incentive to service debt on a timely basis has weakened over the past few years. Since 1981, the spread between debt troubled countries' new borrowings and interest payments has narrowed sharply. For many LDCs, interest payments have risen while their ability to obtain new loans has declined. For some 20 key debtors taken as a group, for example, new medium- and long-term loans exceeded interest paid by an amount equal to 3 percent of their GDPs in 1974-79; in 1980-83, this difference had declined to about 1 percent of GDP.

From an individual country standpoint, a number of debtors recently have had to pay more in interest

25X1

25X1

25X1

ا 25X1

25**X**1

. I 25X1

Foreign Trade Dependence—A Closer Look

Of the economic deterrents against a decision to stop principal and interest payments on debt, the prospect of trade disruption probably is the greatest. The size of this deterrent depends on the importance of foreign trade to a country. Although imports as a share of GDP is a crude indicator of the potential costs associated with a severe disruption of trade, it is useful in suggesting relative differences among countries. United Nations statistics show that, of the major debtors, Taiwan, Malaysia, Venezuela, Algeria, and South Korea rely the most on foreign trade. For these five countries, imports as a share of GDP range between 25 and 55 percent. Simply from a trade standpoint, therefore, we would expect these countries to have a strong incentive to promote policies that ensure debt obligations are met and access to foreign credit is maintained. In fact, the East Asian debtors above have an economic policy record that emphasizes economic growth, expansion of exports, and only moderate government intervention. During 1981-83, IMF statistics point to real growth rates in each country of 5 to 6 percent despite the contraction of world trade. Venezuela and Algeria have an oil supply safety

Brazil, Mexico, Argentina, and India are at the other end of the spectrum, with imports—about 10 percent of GDP—being relatively less important to their economies. With its high share of official debt and low interest burden, we do not believe India represents a financial risk. The other countries in this group, however, are in serious financial trouble. Moreover, since 1980 the economies of Brazil, Mexico, and Argentina have all suffered severe recessions accompanied by high inflation, have recently paid more in interest than they have received in new lending, and have a high share of commercial bank debt.

charges than they have been able to obtain in new loans. In 1983, for instance, we estimate that:

- Mexico's interest payments exceeded new borrowing by about \$3.1 billion or nearly 1.2 percent of its GDP.
- Brazil, Argentina, Venezuela, and Chile also experienced significantly greater interest outflows than loan inflows, with the amounts ranging from \$0.5 to \$1.8 billion.

25X1

25X1

The countries that experienced the most adverse shifts in their interest burden also had the highest proportion of foreign debt from private sources. This debt generally carries floating interest rates. By 1983, Latin American countries, in particular, had been hit with a sharp growth in interest payments, reflecting the large percentages of private loans to their countries: Brazil (89 percent), Mexico (85 percent), Argentina (93 percent), Venezuela (99 percent), and Chile (90 percent). These large shares reflect their relatively high per capita income, which in the mid-1970s made them appear to be relatively good credit risks and restricted their ability to secure official development loans. At the opposite end of the spectrum, about 90 percent of India's and Pakistan's medium- and long-term debts are from official sources. Thus, India and Pakistan have been sheltered from the sharp rises in market rates of interest after 1979.

Future Trends

Although a comparison of interest payments and new lending over the last few years suggests that certain major debtors have a weaker incentive to stay current on their debt obligations, the situation is not likely to remain static. Interest rates, in particular, could change as could bankers' and other creditors' views about LDC credit risks. Moreover, future interest charges also will depend on the level of new loans extended.

Major LCD Debtors:

Trends in Interest Payments and New Borrowing, as a share of GDP ^a Percent

	1974-79	1974-79				•
	Net New Borrowing	Interest	Difference	Net New Borrowing	Interest	Difference
Algeria	10.3	2.7	7.6	-0.6	3.7	-4.3
Argentina	2.4	0.9	1.5	3.2	2.2	1.0
Brazil	3.6	1.2	2.4	2.3	2.6	-0.3
Chile	4.9	2.4	2.5	6.0	4.8	1.2
Colombia	1.3	0.9	0.4	2.6	1.3	1.3
Egypt	8.3	1.1	7.2	4.8	2.0	2.8
India	1.0	0.3	0.7	0.7	0.3	0.4
Indonesia	4.0	1.0	3.0	2.7	1.5	1.2
Malaysia	3.5	1.1	2.4	9.3	2.7	6.6
Mexico	5.2	1.7	3.5	2.7	2.5	0.2
Morocco	8.5	1.4	7.1	5.7	4.7	1.0
Nigeria	0.8	0.2	0.6	2.6	1.2	1.4
Pakistan	. 4.5	1.0	3.5	1.3	0.9	0.4
Peru	6.3	2.6	3.7	3.7	4.1	-0.4
Philippines	4.0	1.1	2.9	3.9	2.2	1.7
South Korea	5.3	1.4	3.9	4.0	2.9	1.1
Taiwan	2.3	0.9	1.4	1.7	1.3	0.4
Thailand	2.4	0.6	1.8	4.2	1.9	2.3
Venezuela	4.1	0.9	3.2	3.0	2.8	0.2

^a These figures represent averages for the selected periods and cover medium- and long-term debt only.

To examine the relationship between interest payments and new lending in future years, we have established two scenarios that we believe bound a reasonable range of outcomes. Our projections in Case A are based on favorable financial conditions for the LDCs, and Case B is based on pessimistic conditions:

 Case A assumes that banks and other creditors extend sufficient new credit to allow the countries to increase their debt by 10 percent a year about the rate of increase in 1982-83—and that by 1987 interest rates fall by 25 percent from 1983 levels. Case B assumes that only enough credit is extended to allow the countries' debts to rise 5 percent a year and that interest rates do not decline from 1983 levels.

In both cases, economic growth in the countries examined is assumed to recover gradually by 1987 to one-half of the average rate of the 1970s, and world inflation is assumed to be 5 percent a year.

25X1

25X1

25X1

25X1

25X1

The results of these two scenarios suggest several conclusions:

- Under the favorable assumptions in Case A, for most of the countries in our sample, the interest burden would be roughly matched by new lending over the next several years. Under these circumstances, there would be little change in the incentive for these countries to meet their debt obligations, compared with the current situation.
- Under the less favorable conditions in Case B, interest payments for all of the countries examined would exceed new borrowing during the entire 1984-87 period. The projected gaps would average about 1.0 to 1.5 percent of GDP for most countries. Under these circumstances, we believe there would be a definite weakening in the incentive for these countries to make timely debt service payments.

Outlook

We believe the debt-troubled LDCs will remain reluctant to take drastic steps such as an extended payments moratorium on both principal and interest on financial grounds. The potential costs of such a move—suspension of trade credits, trade disruption, seizure of assets, drying up of foreign investment flows; and loss of official funding—place a powerful restraint on such action. More likely these LDCs will pursue more aggressively such midway measures as negotiated payment moratoriums and running arrearages, as they attempt to realize lower current debt charges while avoiding the penalties of a full moratorium.

Nonetheless, there remains a small risk—which could grow—that one or more of the countries facing continuous capital outflows will respond to domestic political pressures and undertake a moratorium. Such domestic pressures could be sparked by unrest or changes in government—both possible results of more severe economic conditions. Moreover, a moratorium by one debtor could trigger a chain reaction, causing others to follow suit.

. . . .

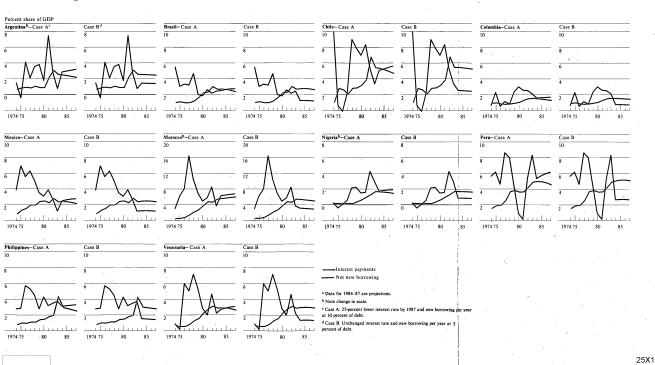
Secret
29 June 1984

28

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000707060001-2

Secret

Selected Major LDC Debtors: Projections of Interest Payments and Net New Borrowing, 1974-87^a



International Financial Situation: Political Update

25X1

IMF austerity measures have led to heightened political tensions in a number of Latin American countries this past month. Labor strikes broke out in Jamaica and Peru, while Honduras, Guatemala, and the Dominican Republic abandoned IMF recommendations in the face of growing political opposition. In Bolivia and Argentina, fragile labor agreements are in jeopardy, and renewed strike activity is likely if new labor demands are not met. In the Philippines, President Marcos this month moved to undertake unpopular austerity measures. in the hope of obtaining a speedy IMF agreement before the opposition can be seated and organized in the new assembly. Mexican President de la Madrid obtained another moderate wage settlement and skillfully undermined leftist efforts to organize antiausterity demonstrations.

In Jamaica, Central Bank and public utility workers have gone on strike to protest strict wage guidelines, and Prime Minister Seaga's recently announced austerity budget. In Peru, President Belaunde declared a 30-day state of emergency to cope with escalating demonstrations by public-sector employees demanding wage hikes to compensate for rising living costs. Fear of renewed political turmoil could lead both these governments to abandon or ease their austerity programs. In addition, the Belaunde administration faces a presidential election campaign

dential election campaign

The governments of Honduras, Guatemala, and the Dominican Republic fell out of compliance with their IMF agreements or had negotiations break

down because they declined to implement tax and price increases in the face of adverse political repercussions:

- President Suazo suspended an unpopular sales tax on items including alcohol, cigarettes, and phone service only hours before the Honduran Labor Federation was to strike.
- Guatemalan Chief of State Mejia refused to raise a value-added tax recommended by the IMF to curb imports and reduce current account and budget deficits.
- Fearing an outbreak of violence similar to riots in April over food-price hikes, Dominican Republic President Jorge Blanco declined to implement an oil price increase that the Fund had requested as a precondition to a new arrangement.

Although these measures will ease domestic political tensions in the short run, they will postpone badly needed adjustments and are likely to worsen economic problems in the months ahead. Suspension of IMF disbursements and a deterioration in creditworthiness is likely to result in arrears on debt service and trade accounts. According to the US Embassy, Santo Domingo recognizes it must come to terms with the IMF in order to renegotiate its debt with official and commercial creditors and to qualify for US aid. Some observers consider the arrest of leftist leaders in recent weeks as a sign that the government is preparing to go ahead with IMF recommendations.

25X1

25X1

25X1

Bolivia could again face renewed labor unrest following a 20 June communique by the powerful Bolivian Workers Central suspending its dialogue with the Siles government. The labor union contends that public announcements by the government that its foreign debt will be negotiated violates a recent labor accord by which the government agreed to postpone debt repayments. Although the debt moratorium formalizes an existing policy of delaying interest payments, the announcement was part of a response to labor demands last month ending weeks of strikes that crippled the transportation and banking sectors.

Widespread strikes and internal feuding within the opposition Peronist party has undermined Argentine President Alfonsin's efforts to achieve labor peace, which he believes is an essential ingredient in implementing economic policy and reaching an accord with the IMF and commercial lenders. In an attempt to regain the initiative, Alfonsin has adopted a tougher posture toward labor, and, at the same time, has renewed efforts to reach an agreement with Peronist bosses on a range of economic issues. The union chiefs' demands, however, will certainly be beyond what Alfonsin is willing to concede. Even if an accord is reached, the current labor leadership exercises little control over the more radical rank and file, and continued confrontations are likely.

Philippine President Marcos is seeking to enact unpopular economic policies before the opposition is seated in the new assembly late next month and begins to debate his management of the economy. Early this month, Manila issued a set of monetary, fiscal, and foreign exchange directives designed to win speedy IMF approval of a \$650 million standby loan and to move forward with rescheduling debts to foreign banks and governments. The measures include a 22-percent devaluation of the peso, a 10-percent import surcharge, a 30-percent tax on exporters' windfall profits, and a 5-percent budget cut. The IMF, according to Embassy reporting, believes that the newly announced policies do not include sufficient tax measures and will increase foreign exchange controls, encourage black-market operations, and result in a multiple exchange rate

regime. Although the measures appear to be strong economic medicine, the IMF will require at least six to eight weeks to assess their impact, making an agreement unlikely before late summer. Resolution of the debt crisis could be delayed even further if the IMF decides other measures are needed or if the opposition objects to the austerity program.

In concluding a moderate wage settlement this month, Mexican President de la Madrid again displayed his ability to limit wage increases and successfully implement an IMF program. The midyear agreement allowed minimum wages to go up only 20 percent, less than half of what union leaders had asked for. To help ensure labor's assent, the government agreed to freeze some utility prices and to monitor price controls more vigorously. The wage settlement will strengthen Mexico's bargaining position with bankers in upcoming rescheduling talks. President de la Madrid's tough control tactics and deft political touch thwarted efforts by leftists in early June to organize major demonstrations.

25X1

25X1

25X1

25X1

International	Financial	Situat	tion
Debt Arreara	ges		

25X1

25X1

A large number of developing countries continue to be in arrears on their external debt repayments. At least 54 LDCs and East European nations currently are behind on their debt repayments, slightly more than the record total of 52 at yearend 1983. We estimate the total amount of debt arrearages at midyear 1984 to be \$30-35 billion, the same as at yearend 1983. The \$30 billion arrearage figure is equivalent to roughly 20 percent of scheduled 1984 debt repayments for these countries.

Most of the arrearages are accounted for by a handful of major debtors:

- Poland's debt arrearages are about \$12.5 billion, according to our estimates, including nearly \$8 billion due to Western governments. Poland is in the process of clearing up some of these arrearages as a precondition to begin negotiations with the Paris Club to reschedule 1982-83 obligations. Most of the remaining arrearages are owed to creditors in socialist countries, Latin America, and the Middle East. Warsaw's payments to Western commercial banks are current as a result of the recent bank rescheduling agreement, which is scheduled to be signed in July,
- Nigeria currently has arrearages totaling about \$7 billion, all on short-term trade-related credits, according to press reports. Of this total, \$4 billion is owed to uninsured creditors and is in the process of being rescheduled on a bilateral basis. The remaining \$3 billion, consisting of officially guaranteed trade credits, has not been rescheduled because of the refusal of Western governments to move forward until Lagos successfully negotiates an IMF-supported adjustment program.

- Venezuela's interest payments on public-sector debt now are current, but some \$1 billion in private-sector arrearages remain, according to Embassy reporting. Caracas is in the process of making foreign exchange available for repayment of private-sector interest, but the process has been slow. Clearing of these arrearages is being required by commercial banks before moving forward with a debt restructuring. In addition, principal repayments of \$2-2.5 billion have been frozen under a moratorium that was instituted in March 1983.
- Argentina had about \$5.5 billion in principal and interest arrearages as of mid-June, according to Embassy and press reporting. Argentina has been running interest arrearages in excess of 90 days. Buenos Aires, however, recently made a \$100 million payment of overdue interest and is working with banks to repay by Saturday the remaining \$350 million required to prevent US banks from having to place their Argentine loans on nonaccrual status.
- Philippine debt arrearages have risen steadily since Manila initiated a moratorium on principal repayments in mid-October 1983. Based on IMF data, we estimate that arrearages currently are about \$2.3 billion, of which \$2 billion are principal repayments.

Until a debt restructuring package is completed, however, arrearages will continue to mount.

25X1 25X1

25X1

Countries With External Payments Arrearages in Mid-June 1984

Latin America

Argentina Bolivia Brazil Chile Colombia Costa Rica Cuba

Dominican Republic Ecuador El Salvador Grenada Guatemala Guyana Haiti Honduras Jamaica Mexico Nicaragua Paraguay Peru Venezuela

Africa/Middle East

Benin
Cameroon
Central African Republic
Chad
Comoros
Congo
Egypt
Gambia, The
Ghana

Guinea
Guinea-Bissau
Ivory Coast
Jordan
Liberia
Madagascar
Mali
Mauritania
Nigeria

Senegal Sierra Leone Somalia Sudan Tanzania Togo Uganda Zaire Zambia

East Asia North Korea

Philippines

Vietnam

Western Samoa

Eastern Europe

Poland

Romania

In contrast to these debtors, Mexico and Brazil have made considerable progress during 1984 in clearing up arrearages. Early this year, Mexico paid \$300 million in arrearages on nonrescheduled debt, and private-sector debt reschedulings have been negotiated to eliminate \$2 billion in arrears. These private-sector agreements, however, could still come unglued. Brazil has brought its payments up to date following the signing of its restructuring package in March 1984.

however, Brazil could experience a new buildup of arrearages during second-half 1984 as it attempts to meet stringent IMF targets.

The most important aspect of debt arrearages to US banks involves the delay of interest payments beyond 90 days. Under new US banking regulations that take effect on 30 September, loans must be placed on nonaccrual status as soon as interest payments are more than 90 days overdue rather than at the end of the quarter, as under previous rules. The only major debtor with an immediate problem in this regard is Argentina. Should a deal not be worked out to reduce interest arrearages below the 90-day level by the end of June, several

25X1 25X1

25X1

	Secret
sanitized Copy Approved for Release 2011/03/0	7: CIA-RDP97-00771R000707060001-2

	US banks have publicly stated that they place their Argentine loans on nonaccrual
status.	

25X1

Secret

International Financial Situation:						
Comparison of Adjustment in Eastern Europe						
and Five Major Debt-Troubled LDCs						

25X1

25X1

25X1

25X1

Eastern Europe appears to be adjusting to its debt crisis more rapidly than most of the LDCs. GNP growth in Eastern Europe is projected to approach 2 percent this year—the third consecutive year it has increased. Current account surpluses and the reluctance of lenders have caused some East European countries to reduce their hard currency debts; the region's gross debt at yearend 1983 of \$82 billion is nearly \$4 billion less than the 1981 peak. The small climb in the debt projected for this year reflects not only Poland's accumulating arrearages, but also the renewed ability of other East European countries to attract foreign commercial credits. In contrast, real output in the five key debt-troubled LDCs will drop for the third year in a row. Moreover, current account deficits will continue, and new "involuntary" bank loans arising from restructuring packages probably will add almost \$11 billion to their debt.

Differing Circumstances

Eastern Europe's quicker turnaround results partly from being forced into adjustment earlier than the LDC debtors. Poland's financial problems began in 1980 and were soon followed by Romania's growing arrearages in the summer of 1981. Bankers' doubts about the region's creditworthiness were heightened by the increased chill in East-West relations, which were precipitated by the Soviet invasion of Afghanistan and worsened by the imposition of martial law in Poland. By early 1982, Eastern Europe was experiencing a marked reduction in credit lines, while the Latin American LDCs continued to attract new loans. More than a year

¹ In this article, Eastern Europe includes Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and Yugoslavia, while the five key LDC debtors are Argentina, Brazil, Chile, Mexico, and Venezuela.

before the Mexican and Brazilian payments difficulties surfaced, both Poland and Romania already had rescheduled external obligations, and Yugoslav creditors were putting together a rescue package.

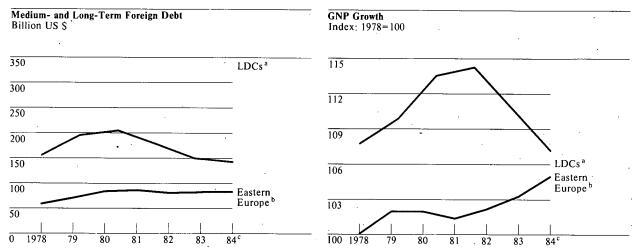
Most of Eastern Europe has benefited by facing comparatively smaller financial problems than the Latin American debtors. The LDCs conduct 80 to 95 percent of their total trade in "hard" currencies and, as a result, are critically dependent on access to foreign credit. Eastern Europe, on the other hand, conducts between 65 and 80 percent of total trade turnover in nonconvertible currencies. This large share reduces the region's dependence on hard currency credits. Within this trade, the Soviet Union provided significant economic support to Eastern Europe—at least through 1982—via large oil price subsidies and the toleration of persistent trade deficits. In comparing hard currency financial strains, the five key LDC debtors were burdened by debt service ratios ranging from 32 to 98 percent in 1982 compared with just 18 to 53 percent in Eastern Europe (excluding Poland).

Impact of Adjustment

Both of these regions have adjusted largely through precipitous import cuts. Hard currency imports declined 25 percent in 1980-82 in Eastern Europe and nearly 50 percent in 1981-83 in the five key Latin American debtor countries. The slide in imports appears to have ended in Eastern Europe, with some growth projected for this year. For the five LDCs as a group, imports will continue to fall this year but at a slower pace than in the two previous years.

25X1 25X1

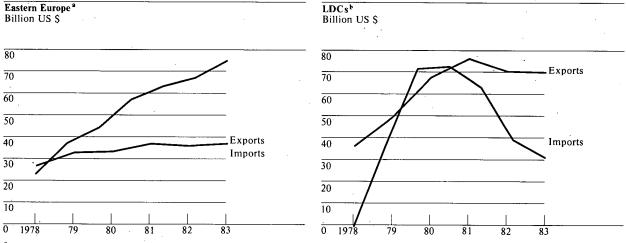
Selected Debt-Troubled Countries: Foreign Debt and Economic Growth



^a Argentina, Brazil, Chile, Mexico, and Venezuela.

303056 (A04817) 6-84

Selected Debt-Troubled Countries: Trade Adjustment



^a Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and Yugoslavia

303057 (A04816) 6-84

Secret
29 June 1984

38

^b Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and Yugoslavia.

^c Projected.

^b Argentina, Brazil, Chile, Mexico, and Venezuela.

The impact on the domestic economies has varied as well. Although economic growth was halted in both regions, the decline in Eastern Europe already has bottomed out and was far less severe than the drop still going on in the LDCs. Indeed, only Poland experienced a severe decline in output that is comparable with the five LDCs.

The East European regimes have attempted to spare consumers from shouldering much of the adjustment burden. Investment bore much of the initial brunt of adjustment, dropping 8 percent a year in 1981-82, while consumption remained relatively constant or declined marginally (again, Poland excepted). Consumers in LDCs have fared much worse, experiencing steady drops in both real incomes and consumption during the past couple of years. This deterioration has sparked unrest and strained the political systems in many of these debtor countries.

Outlook

Despite Eastern Europe's quicker recovery from the credit crunch compared with the LDCs, the region still faces long-term trade and financial problems. The regimes have opted for quick fixes and have done little to correct longstanding problems with export competitiveness. Continuing financial problems in the LDCs are hurting East European sales to these important markets. In addition, broader economic adjustments under way in many LDCs are making these countries more aggressive competitors in world markets. The breathing space provided by debt reschedulings for Poland, Romania, and Yugoslavia will end in a few years. More reschedulings may be required, and creditors are not yet convinced that, over the long term, Eastern Europe represents a more attractive credit risk than the LDCs.

•

25X1

25X1

25X1

Secret

The Soviet Grain Crop: Impact on land Meat Supplies	Imports 25X
The size of this year's grain crop is likely to lead to higher grain imports than in 1983 and could jeopardize the Soviets' effort to match last year's record meat production. Even so, upward pressure on world grain prices probably will be slight. Moscow's Consumer Goals Even in poor harvest years the Soviet Union produces more than enough grain to meet the needs of its people for bread and other grain products. The problem is to also grow enough feed to maintain livestock herds and expand meat production. Boosting meat supplies has been the centerpiece of Soviet efforts to improve the lot of the consumer since the mid-1960s. Moscow needs to increase meat supplies each year by 1 to 2 percent per capita just to keep shopper queues from increasing substantially and to sustain relatively stable meat prices in free markets for another year. During 1979-82, consumers endured lengthening queues and surges in free market prices. It would take several years of marked growth in meat supplies, however, to satisfy pentup demand. This spring's bad weather presumably has raised concerns about future meat supplies and may have caused the flurry of new grain purchases in recent weeks. If the crop is sharply reduced, the Soviet leaders will have to decide whether to incur the additional hard currency cost of larger grain imports or to accept an increase in consumer dissatisfaction.	
The Impact of the Weather It is already clear that this year's grain crop will fall considerably below the 1978 record harvest of	

41

25X1

25X1

25X1

25X1

25X1

·										
ncrease domestic meat production. A reduction in										
nerd size would then be the primary way to raise									•	:
neat output.						,		*		
-		•								
We believe the Soviets would be unlikely to sharply										
educe herds, however, unless the harvest was										
lisastrous—on a par with the 140-million-ton crop										
n 1975. They have invested heavily in rebuilding							ì .			
nerds since the marked reduction in 1975 and										
inderstand fully the problems involved. They										
would see consumer dissatisfaction and price pres-	•									
sures in the near term as less damaging to domestic				٠.						
		•								
stability than the longer term impact of excessive										
ivestock slaughtering.	ì									
						•				
Impact on World Grain Prices. The Soviets would								• .		
have little trouble buying 45 million tons of grain										
or 1984 delivery. If the stepped-up tempo in						٠.				
nonthly deliveries to the USSR—needed to								-		
chieve this estimate—were continued for the bal-									•	
ince of the 1984/85 marketing year (1 July-30	,									
June), imports for that period would be over 50		,								
million tons. Record wheat stocks and bumper										
crops expected in the West probably would offset										
nost of any upward pressure on prices caused by										
such large Soviet purchases. In the event, however,										
of unfavorable weather in another major growing							•			
egion—especially the United States or Canada—										•
or of heavy Soviet grain buying in the near term,										
prices could rise substantially.										
According to international grain traders, the USSR	•			•						
bought as much as 7.5 million tons of grain from										
Canada, Argentina, and the European Community								•	*	
by mid-June as well as 750,000 tons of new-crop										
JS wheat. Deteriorating Soviet crop prospects							-			
probably prompted these initiatives. Grain imports	• '					•				
n 1983 cost Moscow an estimated \$5 billion and										
accounted for almost 20 percent of all Soviet hard		·								
currency imports. Grain imports of 45 million tons					•					
n 1984 would raise the grain bill to over \$6.5			•		•					
pillion.										
7111Q11.	•.									
'					,					
•										



Secret